

Division of Oil and Gas

Indiana Government Center South
402 West Washington Street, W293
Indianapolis, IN 46204

Herschel L. McDivitt

Director

317-232-4058

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**NOTICE OF INFORMAL HEARING ON APPLICATION FOR FORCED POOLING
FILED BY PIONEER OIL COMPANY, INC. – KLOTZ HEIRS DRILLING UNITS****CAUSE NO. DOG-7-2009**

TO: Henry D. Hargrove III, 15702 Cavendish, Houston, TX 77059
Luke A. Klotz, 3996 Englewood St., Jackson, MI 49201
Kazumi I. Blackburn, 2434 Badajoz Pl., Carlsbad, CA 92009
Edward I. Blackburn, 2434 Badajoz Pl., Carlsbad, CA 92009
Sandra B. Jenson, 2434 Badajoz Pl., Carlsbad, CA 92009

Background

Indiana law requires the protection of what are known as "correlative rights." This means that a property owner's opportunity to receive the benefits of the oil, gas and other hydrocarbons located beneath their acreage cannot be rightfully taken away. Any owner of oil and gas interests is entitled to share in the production of oil and gas produced from their property. This may result either from the drilling of a well by the owner or by conveying their oil and gas interests to another party who would then drill a well and allocate a proportionate share of the proceeds from the production to the owner. Most owners choose to lease their oil and gas interests to another party rather than assume the risk and expense associated with the drilling of their own well.

Where owners voluntarily sign an oil and gas lease, the lease agreement establishes the specific terms and payments to be made from production. If an owner has chosen not to negotiate the terms of exploration and production, the compulsory integration process is intended to safeguard their correlative rights. It is our understanding that a representative of the petitioner has made a diligent and reasonable attempt to obtain your consent to the leasing of your oil and gas interests as documented in EXHIBIT "D" of the Petition.

In order to prevent waste of oil or natural gas and the drilling of unnecessary wells, Indiana regulations also place restrictions and requirements upon any operator drilling a well for oil and gas purposes. According to 312 IAC 16-5-1 and 16-5-2, operators are required to form a drilling unit, also known as a spacing unit, of sufficient size, so as to effectively and economically drain all of the oil or gas resources thereunder, while minimizing the environmental impact.

Indiana Law, at IC 14-37-9, spells out the requirements for the voluntary and involuntary integrating of oil and gas interests among different owners within an established drilling unit. Integration occurs voluntarily when all property owners within a spacing unit execute an oil and gas lease containing a pooling clause in favor of a single developer or well

operator. The law also allows for the integration of interests in instances where not all of the oil and gas interest owners have executed a lease. This process is sometimes referred to as “forced pooling”.

Accordingly, a well operator may submit a petition for involuntary integration to the Division of Oil and Gas whenever the integration of interests is necessary in order to prevent the stated statutory purposes of avoiding waste and preventing the drilling of unnecessary wells. Prior to submitting a petition, a well operator is required to obtain a substantial majority of the interests within the drilling unit and must also have made a diligent and reasonable attempt to obtain the consent of all owners of oil and gas interests within the drilling unit.

You are being provided with this notice because a petition has been submitted to our office on behalf of Pioneer Oil Company, Inc., requesting that certain interests owned by the following:

- Henry D. Hargrove III, 15702 Cavendish, Houston, TX 77059;
- Luke A. Klotz, 3996 Englewood St., Jackson, MI 49201;
- Kazumi I. Blackburn, 2434 Badajoz Pl., Carlsbad, CA 92009;
- Edward I. Blackburn, 2434 Badajoz Pl., Carlsbad, CA 92009;
- Sandra B. Jenson, 2434 Badajoz Pl., Carlsbad, CA 92009;

be incorporated into the above described drilling or spacing unit. The unleased interests are located in the East Half of the Southwest Quarter (E ½ of SW ¼) of Section 7, Township 8 South, Range 13 West, in Posey County, Indiana.

A copy of the petition is included for your review. Copies may also be viewed from our website at <http://www.in.gov/dnr/dnroil>. Click on the “Informal Hearing Schedule and Final Orders” icon to view a table of upcoming informal hearings. A hyperlink to the petition can be viewed by selecting ([View Petition](#)) hyperlink for this cause number (DOG-7-2009).

In considering the petition the Division of Oil and Gas must ensure that owners receive an equitable share of the oil and natural gas produced from the integrated drilling units. For primary production wells, owners usually are assigned a percentage share based upon the ratio of the acreage you own and the total acreage in the unit. For example a 25 acre parcel which was part of a 100 acre unit would be assigned a 0.25 or 25% interest in the oil or gas production multiplied by a factor which reflects the specific oil and gas interests which the owner possesses (i.e. royalty interest, working interest, over-riding royalty interest, etc.).

Your Options

It is important to understand that, at any time, should you decide to voluntarily sign a mutually acceptable lease with the petitioners, there will be no need to proceed further with this process to integrate your interests.

Since your interests are located within drilling units duly established pursuant to Indiana regulations, and integration terms have not been agreed upon through a lease, the forced

pooling or integration procedure provides you with three (3) options regarding the distribution of production from within the drilling units. Note that an integration order in this instance will usually not grant to the operator a legal right of entry onto, over, or across the surface of your property. Your choice relates only to how you would prefer to receive production proceeds and whether you want to increase your portion by sharing in the associated costs of the well. A summary of your options is as follows:

1. **Integration as a Royalty Owner**: If you elect this option, you are not liable for any costs or fees associated with the well operation. ***This is the default option that we will select for you if we do not hear otherwise from you.*** As a royalty owner you will be entitled to receive not less than 1/8th of the net production of oil, gas and other hydrocarbons above that which may be used or consumed for production or development purposes. The net production share is based upon the ratio between the acreage of the tract you own and the total acreage of the spacing unit.
2. **Integration as a Participating Owner**: If you elect this option, you can participate in the costs of drilling and production by paying your share of estimated well costs to the well operator within thirty (30) days of the informal hearing. This money will not be refunded if the well is a dry hole or does not pay for itself. In exchange, you will receive your full proportional share of the production.
3. **Integration as a Non-Participating Owner**: If you elect this option, you can participate in the costs of drilling and production on a limited or carried basis. You will have the same responsibilities as a participating owner, except that you do not risk your own money by paying your share of costs up front. A dry hole costs you nothing. You will not receive compensation from the well operator until the well operator has, through the sale of your share of production, recovered your proportional share of the costs for drilling and operating the well. Thereafter, you will receive your proportional share of the production and will be treated as a participating owner.

Most owners choose not to participate in the drilling and operational costs of a well and are integrated as a ***royalty owner (Option 1)***. If you are interested in pursuing integration as either a ***non-participating owner (Option 2)*** or a ***participating owner (Option 3)***, you will need to contact the petitioner to obtain information regarding the estimated well costs and operating expenses that you would be expected to share.

You are encouraged to consult with a lawyer experienced in oil and gas leasing before making any decisions. In most cases, you will be choosing among your options before the well is drilled and before you know whether the well will be a success that pays for itself, a marginal producer that never pays for itself, or a dry hole. Investing in oil and gas exploration can be a risky proposition and the benefits, costs, and obligations of participating in an oil or gas well may affect you and your property for many years.

Notice of Informal Hearing – Cause No. DOG-7-2009

An informal hearing to consider the petition and receive comments from interested persons is scheduled for Thursday, December 17, 2009, at 11:00 a.m. (Eastern) at the Indianapolis

Office of the Division of Oil and Gas, located at 402 West Washington Street, Room W293, Indianapolis, IN 46204. The telephone number at this office is (317) 232-1550. This hearing is being conducted as required by IC 14-37-3-16(4) and 312 IAC 16-2-3.

Again, you are reminded that at any time prior to the integration hearing, you may voluntarily enter into a lease or other private agreement regarding the development of your oil and gas resources.

If you have questions pertaining to the petition, the informal hearing process, or any of your options described above, please contact me at 317-232-4058 or by e-mail at hmcdivitt@dnr.in.gov. Comments concerning the petition may be submitted in writing to the address below and must be postmarked no later than **December 17, 2009**, in order to be considered:

Herschel L. McDivitt, Director
Division of Oil and Gas
Department of Natural Resources
402 West Washington Street, Room W-293
Indianapolis, IN 46204

Interested persons may attend the informal hearing and present relevant oral or written comments in person or by counsel. After reviewing all oral and written comments received, the Division will either approve or deny the Petition for Integration of Interests filed by Pioneer Oil Company, Inc. in a written order that will be subject to administrative review under Indiana Code 4-21.5.

November 18, 2009

DATED



Herschel L. McDivitt
Director
Indiana Division of Oil and Gas